IT 98-0055 GIL 06/29/1998 SUBTRACTION MODIFICATIONS - PENSIONS

General Information Letter: Illinois tax treatment of employer and employee contributions to and distributions from qualified pension plans.

June 29, 1998

Dear:

This is to acknowledge receipt of your recent letter. Therein, you request the completion of the attached surveys concerning retirement and deferred compensation plans. Specifically, the surveys ask a series of questions concerning the Illinois income tax treatment of retirement and deferred compensation plans.

In your letter, you ask whether Illinois' guidelines default to federal guidelines, without exception. With respect to contributions, this is an accurate statement. Please note that Section 203 of the Illinois Income Tax Act ("IITA") provides that "in the case of an individual, base income means an amount equal to the taxpayer's adjusted gross income for the taxable year as modified by paragraph 2." (See IITA Section 203, copy attached hereto) The reference to adjusted gross income is a reference to federal adjusted gross income. This figure is subject to certain addition and subtraction modifications specifically set forth in Section 203(a)(2). Regarding distributions, it would therefore not be accurate to simply respond we default to federal guidelines. There are some differences, particularly with reference to retirement income.

Section 203(a)(2)(F) of the IITA provides a subtraction modification from federal adjusted gross income for an amount equal to all amounts included in such total pursuant to the provisions of Sections 402(a), 402(c), 403(a), 403(b), 406(a), 407(a), and 408 of the Internal Revenue Code, or included in such total as distributions under the provisions of any retirement or disability plan for employees of any governmental agency or unit, or disability plan for employees of any governmental agency or unit, or retirement [payments to retired partners which payment are excluded in computing net earnings from self-employment by Section 1402 of the Internal Revenue Code and regulations adopted pursuant thereto.

With regard to withholding, although state withholding requirements generally parallel federal requirements, as noted above, Section 203(a)(2)(F) provides a subtraction modification from base income for certain retirement plans, disability plans, and pension distributions. As a result, state withholding is not required with respect to these amounts. Keeping this statutory basis in mind, provided below are responses to the questions presented in your surveys. Given the general nature of your questions, the Department's responses are, of necessity, quite general. You should caution your readers that they should utilize these answers only for general background information and with respect to specific situations, they may wish to seek further guidance from the Department by requesting private letter rulings or general information letters as appropriate. Your questions have been reproduced below and the Department's replies follow your questions and are distinguished by bold face type.

TAX TREATMENT OF EMPLOYEE CONTRIBUTIONS TO RETIREMENT AND DEFERRED COMPENSATION PLANS (emphasis added)

1. 401(K)-Qualified cash or Deferred arrangement is part of a profit sharing or stock bonus plan (or any qualified plan).

Reply: Section 401(k) before-tax salary deferrals in the year of deferral are not a part of federal adjusted gross income and are not added back in determining Illinois base income subject to Illinois income taxation.

2. 403(b)-Tax sheltered annuity contract that is purchased under a qualified plan covering certain employees of education institutions and tax exempt organizations.

Reply: Section 203(a)(2)(F) of the IITA allows a subtraction from federal adjusted gross income in determining Illinois base income for all amounts included within the provisions of IRC 403(b).

3. 408(k)-A simplified employee pension which can include a salary reduction arrangement where an employee elects to make pre-tax contributions.

Reply: As indicated above, Section 203(a)(2)(F) of the IITA provides a subtraction modification for an amount equal to all amounts included in federal adjusted gross income pursuant to the provisions of Section 408 of the IRC.

4. 414(h)-Employer pick up plans. Government plans that are "picked up" by the employer are treated as employer contributions. A contribution is picked up if it is made in the employee's name but the employee is never actually charged for it. Trust or annuity plans.

Reply: So long as these contributions are not included in federal adjusted gross income, it does not appear that such contributions are subject to one of the addition modifications of Section 203(a)(1) and as a result will not be included in Illinois base income.

5. 457-A deferred compensation plan for employees of state and local governments and tax exempt organizations.

Reply: Section 203(a)(2)(F) of the IITA provides a subtraction from federal adjusted gross income in determining an individual's Illinois base income for government plans, but not for exempt organization plans under IRC 57.

6. 501(c)(18)-A trust which is part of a pension plan that is funded by employee contributions only. The plan should have been established prior to July of 1959.

Reply: To the extent that these amounts are not included in federal adjusted gross income, it does not appear that the amounts will be a portion of Illinois base income.

7. Simplified employee pension plan "simple" established under Section 408 of the IRS Code.

Reply: Pursuant to Section 203(a)(2)(F), there is a subtraction modification from federal adjusted gross income in determining an individual's base income for such amounts.

8. Simplified employee pension plan "simple" established under Section 401 of the IRS Code.

Reply: See #7.

9. Unfunded, unsecured non-qualified deferred compensation plan where there is: no risk of forfeiture/substantial risk of forfeiture.

SERPS

Rabbi Trust

Secular trust

Corp. Owned Life Ins.

EE Purchase Plan

Reply: To the extent that these items are a portion of federal adjusted gross income, they will be used in determining Illinois base income, which is used in determining liability for Illinois tax.

10. Funded, nonqualified deferred compensation plan where there is: no risk of forfeiture/substantial risk of forfeiture.

SERPS (executive)

Rabbi Trust

Secular Trust

Corp. Owned Life Ins.

EE Purchase Plan

Reply: See #9.

Employer Contributions

1. through 8. (tax qualified retirement or deferred compensation plan).

Reply: As indicated above, Section 203(a)(2)(F) of the IITA provides a subtraction modification for those amounts included in federal adjusted gross income which are covered by the aforementioned provisions of the IRC.

9. Non-qualified deferred compensation plan - funded.

Reply: To the extent that these items are a portion of federal adjusted gross income, they will be used in determining Illinois base income, which is used in determining liability for Illinois tax.

10. Non-qualified deferred compensation plan - unfunded.

Reply: To the extent that these items are a portion of federal adjusted gross income, they will be used in determining Illinois base income, which is used in determining liability for Illinois tax.

If you have any questions regarding the responses provided above, please feel free to contact our office.

Very truly yours,

Jackson E. Donley
Associate Counsel